

ORIGINAL

DIVISION OF CONSUMER ADVOCACY
Department of Commerce and
Consumer Affairs
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Honolulu, Hawaii 96813
Telephone: (808) 586-2800

BEFORE THE PUBLIC UTILITIES COMMISSION
OF THE STATE OF HAWAII

FILED
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PUBLIC UTILITIES
COMMISSION

In the Matter of the Application of)
)
PUBLIC UTILITIES COMMISSION)
)
Instituting a Proceeding to Investigate)
Implementing a Decoupling Mechanism for)
Hawaiian Electric Company, Inc., Hawaii)
Electric Light Company, Inc., and Maui)
Electric Company, Limited.)

DOCKET NO. 2008-0274

DIVISION OF CONSUMER ADVOCACY'S
RESPONSE TO THE PUBLIC UTILITIES COMMISSION'S INFORMATION REQUEST

Pursuant to Commission's letter, dated June 5, 2009, the Division of Consumer Advocacy submits its **RESPONSE TO THE PUBLIC UTILITIES COMMISSION'S INFORMATION REQUEST** in the above docketed matter.

DATED: Honolulu, Hawaii, June 24, 2009.

Respectfully submitted,

By Catherine P. Awakuni
CATHERINE P. AWAKUNI
Executive Director

DIVISION OF CONSUMER ADVOCACY

DOCKET NO. 2008-0274

PUBLIC UTILITIES COMMISSION

**DIVISION OF CONSUMER ADVOCACY'S RESPONSE TO
THE PUBLIC UTILITIES COMMISSION'S INFORMATION REQUEST**

PUC-IR-49 The current ECAC uses the 2005 energy mix to calculate the ECAC. Does the use of 2005 proportions rather than actual proportions cause the utility to charge more or less than its actual costs when the actual mix is different from the 2005 mix? Does the use of set proportions rather than actual energy mix create a complete pass through? If not, why have you not discussed the proportional allocation as well as the heat rate adjustment? If there have been differences between actual costs experienced and revenues charged to the customers because of the use of the 2005 energy mix, please provide the monetary difference for each year from 2004 through 2008.

Response: For purposes of responding to the above, which appears to contain numerous subparts, the Consumer Advocate will attempt to be responsive to each subpart and will, as a result, re-order the question into subparts.

- a. As a matter of clarification, the ECAC in its current form uses the actual proportions rather than the 2005 mmbtu energy mix proportions. Currently, only the mmbtu/kWh efficiency factor is fixed on the basis of the 2005 rate case, the other inputs to the ECAC calculation (i.e., fuel prices and mmbtu energy mix) are based on actual prices and mix proportions. Notwithstanding this clarification, the Consumer Advocate acknowledges that the use of a fixed efficiency factor value (which is based on the energy mix used in the determination of the ECAC base in the most recent rate case) can potentially result in the utility charging ratepayers for an amount that differs from the actual costs associated with the

differences in mmbtu/kWh efficiency between actual heat rates and the heat rate fixed in the ECAC. As indicated in Exhibit D to the Joint Final Statement of Position of the HECO Companies and Consumer Advocate filed May 11, 2009 ("Joint FSOP"), the heat rate will change when utility generators are taken off economic dispatch to accommodate increased levels of renewable energy, and that the fixed heat rate may incent the utilities to take less renewable energy under certain circumstances. In the Joint FSOP, the HECO Companies and Consumer Advocate jointly proposed that a heat rate deadband be established above and below each of the fixed heat rates. The joint proposal is being supplemented with documents to be filed with the Commission on Thursday, June 25 that will include a final ECAC proposal.

In summary, the joint ECAC proposal provides a reasonable opportunity for the utility to recover actual fuel costs, while maintaining the fixed heat rate concept upheld by past Commission decisions (see response subpart c below for a background perspective of the fixed heat rate used in the ECAC calculation). It is the Consumer Advocate's expectation that if the Commission approves the proposed decoupling rate mechanisms with the joint ECAC proposal, the concerns associated with the potential over- or under-recovery of fuel and purchased power expenses will be somewhat mitigated, while continuing the incentive for the utility to

operate as efficiently as possible through the use of the fixed heat rate concept.

- b. The use of a set or fixed heat rate estimates within the proposed deadband concept, when reconciling charges (or credits) to be passed on to ratepayers will result in a "true" and complete pass through. Under the joint ECAC proposal, if the utility's actual heat rate falls outside of the proposed deadband, the reconciling charges (or credits) to be passed on to ratepayers does not result in a "true" or complete pass through.
- c. The Consumer Advocate assumes that this question is seeking to establish why the fixed heat rate should not be eliminated. To provide a background perspective to this question, the Consumer Advocate would like to offer some history on this matter. It is our understanding that a fixed heat rate was generally used in this jurisdiction when determining the ECAC charge or credit. As it specifically relates to HECO, however, in Docket No. 7700 (1994 test year), the Consumer Advocate's witness at that time recommended that the use of a fixed heat rate be discontinued (see e.g., page 4 of CA-T-4 in Docket No. 7700). The general justification for the recommendation appears to be similar to the contention that appears to be the basis for the Commission's question, that is, if the ECAC is based upon the actual mix rather than a fixed heat rate, then it would be a complete true-up.

(See e.g., page 73 of CA-T-4 in Docket No. 7700). The Consumer Advocate's recommendation was generally predicated upon the assumption that, with this change, "customers [would be] charged the actual prudently incurred costs for fuel and purchased energy - no more and no less." (Page 73 of CA-T-4 in Docket No. 7700). The parties in that docket agreed to eliminating the fixed heat rate and modifying the ECAC, but as will be discussed later, the Commission rejected that agreement.

It should also be noted that HECO then proposed that the fixed heat rate be eliminated in Docket No. 7766, which utilized a 1995 test year, to be replaced by the actual monthly sales heat rate factor. (See, generally, HECO T-2 in that docket). The justification for this position basically consisted of the possible over- or under- recovery that could occur with a fixed heat rate as well as the assertion that the heat rate was a function of the combination of system loads and the amount and timing of purchased energy, and as such, a fixed heat rate does not accurately reflect that mix. Notwithstanding the position that was advocated in Docket No. 7700, in Docket No. 7766, the Consumer Advocate returned to the policy that eliminating the fixed heat rate would not be in the public interest. (See, generally CA-T-4, pages 37 through 45).

As mentioned earlier, as articulated in Decision and Order No. 13704 (Docket No. 7700), the Commission rejected the

agreement reached between HECO and the Consumer Advocate to eliminate the fixed heat rate. As justification for its decision, the Commission articulated that a fixed heat rate

“provides a financial incentive for HECO to more efficiently manage its own generation and dispatch energy produced by IPPs. Without the [fixed] heat rate, the company could recover the cost of the fuel oil expense, regardless of the actual heat rate. With the heat rate, the company incurs a penalty if performance falls below that which had been achieved previously.” (pages 11 and 12 of Decision and Order No. 13704)

The Commission's discussion continued by observing that the elimination of the fixed heat rate could result in the perverse incentive for a utility company to forecast a certain level of maintenance expenses to be recovered through base rates and then allowing actual maintenance expense fall below the projected level included in base rates, which could subsequently result in the actual heat rate degrade. Thus, if the company was allowed to recover the actual fuel/purchased power costs through the ECAC (i.e., without a fixed heat rate), a company could game the system to its benefit. The Commission recognized that, even with certain reporting procedures, the company would essentially be receiving a windfall through the customers' subsidization of the company's inefficiency.

The Commission's position in that Decision and Order is consistent with the policy that has guided the Consumer Advocate's

recommendations regarding the heat rate in most of the Consumer Advocate's filings on this matter. That is, a fixed rate can be used to encourage the electric utility company to efficiently dispatch its various generation resources by setting a heat rate that represents an achievable rate, but also represents an efficient dispatch of available resources. Furthermore, a fixed heat rate developed in the test year helps to maintain the relationships among the revenue requirement that is established with the various revenue requirement elements.

For instance, suppose a utility company argues that it should be allowed to recover capital costs associated with a planned generating unit to be added in the test year that should increase the efficiency of the heat rate. If the unit does not go into service and the heat rate is not fixed, the company would be able to recover the costs of the plant even though it was not completed in the test year and would also be able to recover the actual heat rate, which would reflect a less efficient factor and higher overall costs. This situation, similar to the potential company imposed constraint on maintenance expense, would essentially result in the company recovering a windfall from customers.

The Consumer Advocate acknowledges that there may be times that a fixed heat rate will result in certain undesirable results. However, this emphasizes the need, even with the proposed

decoupling rate recovery mechanisms currently being offered for the Commission's consideration, for the parties to any ratemaking procedure to develop a heat rate estimate or estimates that represent reasonable, achievable values that incorporate targeted efficiency levels commensurate with the various revenue requirement elements that will be recognized in that particular test year.

Finally, on June 2, 2006, the Governor of Hawaii signed into law Act 162 that requires the Commission to consider whether a utility's ECAC provides sufficient incentive to reasonably manage or lower its fuel costs. The HECO Companies' ability to recover its fuel expenses is subject to the efficiency factor embedded in the ECAC.

- d. The Consumer Advocate has not attempted to calculate the estimated difference between the actual costs experienced and revenues charged to customers based on fixed values. Based on the Commission's PUC-IR-43, it appears that HECO, HELCO, and MECO will provide the estimated over/under collections based on its calculations. The Consumer Advocate would like to reserve its rights to comment on the reasonableness of these estimates.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing **DIVISION OF CONSUMER ADVOCACY'S RESPONSE TO THE PUBLIC UTILITIES COMMISSION'S INFORMATION REQUEST** was duly served upon the following parties, by personal service, hand delivery, and/or U.S. mail, postage prepaid, and properly addressed pursuant to HAR § 6-61-21(d).

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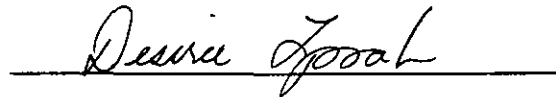
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DATED: Honolulu, Hawaii, June 24, 2009.

A handwritten signature in cursive script, appearing to read "Desiree Zook", is written over a horizontal line.